Subject: **Counter Comments by Vodafone Idea Limited (VIL) to Consultation Paper dated December 17, 2019 on tariff issues related to telecom services**

Dear Sir,

This is with reference to the Consultation Paper on tariff issues related to telecom services, issued by TRAI on December 17, 2019. Comments on the Consultation Paper were uploaded by TRAI on its website for counter comments on March 04, 2020.

There are a number of stakeholders including Government bodies, Telecom Operators, Vendors and Industry Associations who have all supported the need for introduction of floor price. Some of the consumer associations and individuals have also supported the need for the same. The suggestion for floor price reflects that by and large, stakeholders have recognised that there is a serious financial stress in the telecom sector in India.

It is evident from many stakeholders' comments that Floor Price is the need of the hour so that sector can revive. VIL submits that any such floor price fixation must ensure that all the current financial stress is suitably addressed, so that all existing operators are able to sustain their operations in long run based on a return on investment sufficient to invest for future technologies while maintaining optimal competition in the market. Any delay in implementation of the floor pricing will result in irreparable damages including compromised competition or the industry becoming a virtual monopoly which will not be in the interest of consumers or the Government.

Therefore, the underlying objective of the current consultation being revival of all existing players in the market, if any floor price is decided that does not achieve such objective then such an exercise will not only be futile but on the contrary will be completely against consumers' interests as they will not only be deprived of the competition with reduced options and higher charges over time. It is submitted that VIL has shared its detailed costs and working with TRAI and that working results in cost per GB of data at Rs. 34.8 (excluding GST) after adjusting for subscription fee and voice revenue as suggested.

VIL submits that forbearance has resulted in race to bottom as far as tariffs are concerned. In recent past such forbearance has resulted in free / unsustainable below cost service offerings for fairly long period of time by one operator followed by unlimited packs unforeseen anywhere in the world. The forbearance, in such manner, has only resulted in exits of players from the market who paid the ultimate price of such tariff wars. Hence, lack of any floor price in the past has acted as a weapon to drive out the players from the market. Therefore, in the last over three years forbearance has fatally damaged the industry and will hurt the consumers in a more severe and definitive manner if allowed to continue and if correct floor pricing fixation is not implemented at the earliest. Till now the forbearance in such manner had adversely impacted quality of service but if it is allowed any further to continue then it will result in deprivation of connectivity to a large subscriber base. As said by Niti Aayog, floor

prices are absolutely necessary to avert lasting damage to India's digital agenda and economic growth.

Some stakeholders have expressed concerns with the regard to the proposal of introduction of floor tariffs. For the fundamental reasons mentioned above, VIL believes that the apprehensions are misplaced under the current scenario where the industry faces an unprecedented and huge existential and financial crisis, due to underlying issues of low tariffs and resultant market failure. As VIL has previously mentioned in the comments:

- There is a deep financial stress in the telecom sector reflecting in unprecedented decline in revenues, significant losses at the Earnings before Interest Tax (EBIT) level and negative returns on assets/ capital employed over an extended period of time. Except one, all TSPs have a negative rate of return on capital employed.
- Revenues have declined due to sharp decrease in Average Revenue per User (ARPUs) despite the growth in traffic. While the ARPUs have declined by 41% during the period June 2016 to June, 2019, cost pressures in the same period have increased as the voice traffic per subscriber per month increased from 377 to 701 minutes and the data traffic per subscriber per month increased from 0.1 GB to 9.8 GB.
- As a result, the AGR has reduced by 33% over the last three years and is currently at the levels equal to that prevailing in 2012-13.

Forbearance has resulted in unsustainable business models or has encouraged models that are leading towards monopoly situations.

It is reiterated that the telecommunications market in India has been experiencing intense competition with the entry of new operator in 2016 (despite exit by some players and consolidation in the market). This can be characterized as cut-throat (also known as ruinous or destructive) competition. The Organisation for Economic Co-operation and Development's (OECD) defines the same as competition leading to "prices that do not chronically or for extended periods of time cover costs of production, particularly fixed costs", aptly defines the state of the TSPs in India. One of the features of such competition is that the major market player tries to wait until the others withdraw from the market. The price war among TSPs has had a similar outcome with the exit of 6 TSPs. If the policy of forbearance were to continue, then there will be more exits resulting in a virtual monopoly.

The TSPs (and the sector as a whole in the long run) would be better-off if they overcome the current market situation of pricing below cost. In the current market situation, TSPs are unable to adequately increase tariffs to cover costs. The ease of switching across TSPs for consumers (with facilities like mobile number portability, dual sim phones, etc.) makes it further difficult for the TSPs to increase the price to be above costs if some major participant keeps the prices below cost. **Till now the forbearance in such manner had impact on quality of service but if it is allowed to continue any further then it will result in deprivation of connectivity to a large subscriber base, and a price increase over time as TSPs exit the market. The price increase is inevitable and hence it is necessary to do it now, rather than after further exits are forced.**

It is also critical to note that the floor pricing is being considered as a temporary measure till industry revives. There is no other reliable option to provide immediate relief with predictability and stability.

This has been recognised by many stakeholders, including the Niti Aayog which has stated, in its comments dated 4 March 2020, that "**Given the heavy debt burden being faced by the sector and the recent fall in prices to unsustainable levels, there is no option available but to set floor prices.** As we have mentioned in our comments, this may be reviewed for its impact on the market and a view may be taken on bringing back forbearance, once the sector fully revives. **However, in the extraordinary circumstances that the sector is going through at present, we believe that floor prices are absolutely necessary to avert lasting damage to India's digital agenda and economic growth.** TRAI has rightly pointed out that the sector's revenues have not kept pace with the increasing need for investment especially in the context of new technologies like 5G. **It is in national interest to ensure that the sector is provided with much needed relief measures which would ultimately benefit consumers and the economy.**"

VIL's specific response to some of the other comments made by the stakeholders are as follows:

1. ***Comment - Imposition of floor tariffs will impede the entry of new players and level of competition***

   VIL Response:

An apprehension expressed by few stakeholders is that the imposition of floor tariffs will impede the entry of new players and thereby reduce the level of competition.

- **We strongly oppose the above argument as this is against the basic rule of economics – any industry which is profitable will attract new investments and vice versa.** Firstly, it is to be noted that since 2016, 6 TSPs have exited the market and no new operator has entered the market, leaving only three private operators now. The primary reason for such exits is unstainable below cost pricing in the sector. Contrary to above argument, if the floor price is implemented and operators are able to generate reasonable return on investments, the market will become attractive for any new operators to consider entry.
- **Implicit in their comment is the assumption that the only way a new player would enter the Indian cellular service market is with pricing power i.e. large financial resources that allows the new entrant to charge tariffs that are lower than costs.** However, there may be other factors that may be taken into consideration when a new entrant decides to enter a market. For example, in the given situation the negative rates of return on capital will be the far higher and biggest deterrent for any new entrant. Capital flows to the opportunities where the reasonable returns are expected, even if they are not the highest, and not where investors would lose money.
- VIL in its comments has highlighted previously that if floor tariffs are not imposed, then it could lead to further exits and a virtual monopoly. **TRAI may also consider what it would be like to have a virtual monopoly and what will be the fall-out on the consumers including connectivity, prices, security, innovation, impact on Government exchequer and unduly high dependency on one or two players for**

this critical sector which is in nature of an essential service and of critical importance to India's security. *The choice is between "short term tariff correction that are presently below costs and a long term monopoly".*

- The following table provides the consequences with regard to further exit:

Table 1: Competitive Scenario by Service

Service	***No. of subs.***	***No. of current players***	***Are investments being made in this service***	***No. of players in case of further exits***	***Consequences of exit of one private player***
2G and 3G	508 Million	3	No material additional investments	2	• 2G and 3G customers shall be stranded. • Immediate upgradation to 4G by customers will require investments in new handsets • Even then the current capacity of 4G networks may not be adequate
4G	642 Million	3 (BSNL and MTNL are yet to launch 4G services)	Yes	2	• Limited choice for customers • Capacity constraints in 4G networks • Increased demand and reduced supply to increase costs

Importantly, the existing infrastructure which is well laid out will become non-performing while new infrastructure will have to be built to compensate, which will be a poor example of resource utilisation, unduly high costs and customers impacted for few years due to lack of network.

- There are significant barriers to entry in the telecom market in current situation where existing operators with huge investments are in losses. With the exit of most TSPs, a revival of competition in the market would be very difficult. Entry by a new operator, if exit is made by any existing operator, will be very capital intensive and will be exposed to the same risks. The existing investments could also become non-revenue earning. Therefore, the possibility of an exiting player being replaced with a new player is virtually non-existent in such a market.

- **Ensuring that there are no further exits of players is equivalent to entry of a new player.** The loss of resources in case of an exit is very high as equipment worth more than Rs. 100,000 crores will just go out of use, which will be huge waste of capital and resources. This can only result in ultimate increase in cost of the ecosystem.

- The current financial stress and continuation of pricing below the cost has actually resulted in exit of various operators since 2016 as shown below:

Operator	**Year**	**Outcome**
Videocon	2016	Shut down following sale of spectrum to Bharti Airtel
MTS India	2017	Merged into Reliance Communications
Vodafone India	2018	Merged to form Vodafone Idea Limited

Idea Cellular	2018	
Aircel	2018	Declared Bankruptcy
Telenor India	2018	Exited business by Sale of business to Bharti Airtel
Tata Teleservices	2019	Exited business by Sale of business to Bharti Airtel
Reliance Communications	2019	Closed 2G and 3G operations in October 2017. Declared Bankruptcy in 2019

- The request for floor tariffs is being made in the context of financial distress and to ensure that the few current number of TSPs continue to operate. Ensuring continuous operations by incumbent TSPs will ensure that the level of competition does not reduce.
- In any case enough damage has been done to the industry with new entry based on below cost pricing and there is no need for further new entrants whose business model would be based on disruptive below cost pricing in the current situation.

A related issue is an apprehension expressed by some that Floor Prices will end up benefitting inefficient TSPs. While Floor Tariffs are considered, following needs to be taken into consideration:

- As pointed in Table 1, the service offering in not uniform i.e., one TSP offers only 4G services, 2 offer 2G, 3G and 4G services and one offers only 2G and 3G services. 2G services are consumed by a large number of customers in India (close to around 500 million) and therefore TSPs presently have no option but to continue to provide services based on this technology. Given the disparity, it is difficult to ascertain as to which TSP is efficient and which is inefficient.
- **It is important that TRAI recognizes this fact and ensures that those providing non-4G services to over 500 million subscribers can recover their costs**.
- The financial distress is an industry issue and is impacting all the TSPs. While the traffic volumes have exploded, the revenues have decreased. Floor tariffs are proposed in the interim to help the industry overcome the current issues.
- Data tariffs in India are amongst the lowest in the world. Even if the Floor Tariffs were to be implemented, India would continue to have lowest data tariffs in the world. Therefore the question of inefficient TSPs does not arise and is not supported by any data. By this logic if Indian TSPs are inefficient, every other operator in the world would be inefficient.

2. Comment - Floor Tariffs will Impact Innovation

VIL Response:

Some stakeholders have expressed apprehension that floor tariffs will impact innovation. Further, few stakeholders have considered innovation as the ability of the TSPs to “provide tailored plans to different segments of subscribers as per their differential needs and purchasing power”. In this respect it is submitted that:

- Floor tariff is not a prescribed tariff, but just a floor to prevent selling below cost. Further voice rate, subject to certain exceptions, is suggested to be under forbearance. Within the constructs of floor tariff, TSPs are free to design plans for consumers. They can also differentiate their offerings on the quality of service, coverage etc.

- These stakeholders have assumed that the currently prevailing prices are appropriate just because they are under the regime of forbearance. **Comments have been made without an in-depth analysis of the sector and how these prices compare with costs. Market determined prices are however not always pro-competitive as has been recognized by competition law. For instance, competition authorities recognize that even though prices are lower in the short-run and thereby benefit consumers, the possibility of lower competition and higher price in the long run implies that such pricing is anti-competitive. A similar outcome may emerge in the telecom sector if current unviable pricing practice continues and forcing any one or more of the four remaining TSPs to exit the market. In this context it is noteworthy that the Government is supporting the public sector firm by infusion of funds.**
- Innovation has been defined very narrowly. Innovation also refers to India's ability to develop and deploy new technologies such as AI, IoT and related services. **To quote a stakeholder**, "India as a nation needs to invest in the next-generation technologies like 5G, AI, IoT and related services to remain not just competitive with other nations but take leadership position. Telecom sector is the backbone of the exponential growth that Indian economy specially the IT sector has seen in the last decades. India is now one of the leading start-up nation, all these innovations have come on the foundation laid by a robust, growing telecom sector. **The industry would certainly not be able to flourish and invest further in case of a repeat of the earlier price-war situation. We heartily support this TRAI consultation and believe TRAI should come up with a mutually agreeable price-support model for all operators in the eco-system that allows for flexibility for innovative offerings yet supports the telecom sector presently in desperate need for stabilization**."

3. ***Comment - Impact on consumers***

VIL Response -

Number of stakeholders have raised concerns about the impact on consumers. At the outset, VIL wishes to state that Floor Tariffs have been proposed by all TSPs as a temporary measure to stabilise the market. The response to the specific concerns is provided below:

- A stakeholder has commented that "2G services are special as they serve a large segment of low priced service. Any increase in cost to this segment would lead to exit of this section of consumers and have an impact on tele-density of India". It may be noted:
    - 2G consumers are mainly voice only consumers. As per the current proposal, voice rate, with certain exceptions, would generally continue to be under forbearance. This apprehension is, therefore, misplaced. For example, for a low volume 2G user, the extent of offnet voice calls will be only about 200 minutes per month, which would imply a cost of Rs.12 per month, which is insignificant. Hence, 2G subs will not be impacted.

- Further, in case if there is no immediate implementation of the floor price, there could be further exits of a TSP who is currently offering 2G services also. In such scenario the 2G consumers may be left without connectivity, considering that only two players will be left with 2G technology, out of which the government operator is also under severe financial distress with constant need for government funding as their operations incur cash losses in a market with very low tariffs. **BSNL incurred a loss of approx. Rs. 14,900 crores in FY19, its loss for 9 month period between April 19 and December 19 is Rs.39,000 Cr and as per the budget government is expected to infuse over Rs. 37,500 crores in BSNL and MTNL.** Further, the combined capacity of these 2 remaining operators would not be adequate to meet the current demand. Please see Table 1.

- There is a comment that the floor price would limit TSPs flexibility to provide customised consumer plans, tailored for different segments, which enables them to even out costs while maximising quality of service and expand the reach of their networks. It may be noted :
  - As has been mentioned, elsewhere in the response, floor tariff is not a prescribed tariff, but just a floor. Within the constructs of floor tariff, TSPs are free to design plans for consumers. They can also differentiate their offerings on the quality of service, coverage etc..
  - In the long run, the benefits from such a measure (in terms of consumer choice, better quality and technology) are likely to exceed the short-run benefit resulting from consumers paying a lower price in a market with financial distress for the TSPs. This is already reflected in the current consumer experience, where the traffic congestion in networks driven by extremely low tariffs below costs are resulting in unsatisfactory consumer experience.
- A stakeholder has commented, “Floor tariff will have a ripple effect on the affordability of data.” It may be noted:
  - **While the consumers may enjoy lower tariffs in the short run, however, there is no certainty that tariffs would continue at current levels in the future, especially given the possibility of a virtual monopoly in an industry where high capital requirements imply a large entry cost and need for further investments. It would be futile to assume that lower tariffs could be provided indefinitely through subsidies from shareholders/ capital dumping. In fact, it is obvious that prices / consumer spends would go up in such a scenario.**
  - Affordability has always to be defined based on prices which reflect cost. A below cost pricing regime cannot define affordability. In fact given the state of the industry, the cost of capital is very high and will improve once the industry stabilizes as a result of floor price introduction.
- Apprehension has also been expressed regarding the impact of Floor Tariffs on data usage. However, the following needs to be considered:

- It is in the TSPs' interest to work towards increasing the amount of data usage in India. If the data consumption were to be stagnant, then their business would stagnate;
- Tariffs for data services need to cover the costs including cost of capital. It is nobody's case that data usage in India is sustained by forcing TSPs to provide services at a loss;
- As stated above, while the consumers may enjoy lower tariffs in the short run, however, there is no certainty that tariffs would continue at current levels in the future;
- Furthermore, the financial state of the industry also affects the quality of the service. A below-cost tariff situation will lead to incremental deterioration of quality, lack of investment and increasing gaps in the provision of sustained good quality service; and
- Per capita data usage is already amongst the highest in India and some of it represents wasteful usage driven by unlimited plans, which is adversely impacting the consumer experience due to congested networks.

While TRAI evaluates this issue, it may be kept in view that provision of mobile data is a service and needs to be paid for. In an analogous situation, as commented upon in the paper, The Consequences of Treating Electricity as a Right", [1] not paying for cost of providing electricity has hurt the interests of the poor people as they either don't get electricity at all or the quality is very poor. Given that tariffs are lower than costs, similar challenges exist for the Indian telecom sector. **In addition to competitive prices, consumers also need good quality service and the latest technology. A dynamic rather than a static view should be taken by the policy to generate growth and stability in a major strategic industry like telecom with widespread economic and social impact. To protect the interest of the consumers, TRAI must ensure that there are adequate number of TSPs.**

4. Implementation of Floor Prices will dis-incentivise the TSPs to reduce costs

VIL Response-

One apprehension expressed by some of the stakeholders is regarding the incentives on TSPs to reduce costs. We have the following to state:

- The existing players are facing losses despite having taken various cost saving measures, including reduction in cost through realisation of synergies post-merger as in case of VIL. Despite it, they are facing continuous huge losses as the tariffs are well below costs. Hence, the comment is more theoretical in nature as the immediate need is the revival.
- **Floor price are proposed as a temporary measure to stabilise the market. Therefore, incentives on TSPs to reduce costs would continue as forbearance is expected to prevail in the long term.** Furthermore, the floor price is only for a part of the tariff regime,

[1] https://pubs.aeaweb.org/doi/pdfplus/10.1257/jep.34.1.145

and the intense competition will continue to prevail in the market in general. This apprehension is therefore misplaced.

- TSPs have been and continue to undertake measures to optimize costs (including the consolidation that has taken place in the industry in recent years).
- Number of stakeholders have also pointed out that there is an opportunity to reduce regulatory costs. According to one of the Stakeholders "The industry has been bleeding due to over-burdening with plethora of levies and fee(s) imposed over the TSPs." Another stakeholder has commented "To ensure that the sector remains financially viable there are only two options. One is to reduce costs or the other is to increase revenues. To prevent India falling behind other nations and regions when it comes to rolling out 5G, policymakers need to adjust spectrum and infrastructure policies to alleviate the financial burdens on mobile operators including reducing the prices of access and backhaul spectrum and reducing regulatory hurdles to site buildouts. However existing rules and policies give very little leeway for the government or regulator to take above measures. The only option left is to look at increasing the revenues through a floor price mode"
- VIL has taken and continues to take all measures to reduce its costs constantly to be able to provide most competitive services. This is in addition to cost efficiencies obtained through the merger and the ongoing integration. Over a period of last 33 months, between FY17 and Q3FY20, VIL has reduced its operating expenses (excluding license fee, spectrum usage charge and roaming and access charges) by around Rs. 9,500 crores on an annual basis. VIL has taken further measures like rationalization of tower infrastructure, simplification of the tariff plans resulting in lower servicing cost and customer acquisition cost etc.

To conclude, TSPs continue to reduce costs and have even undergone mergers. Nowhere in the world is there a situation where the number 2 and number 3 player in telecom sector and having nearly 30% market share, which is a large scale of operation, continue to incur losses on a quarterly basis for extended period of time.

Considering that the poor financial health is on account of erosion of revenues, immediate correction on revenue side is utmost required for any remedy to be effective. The damage to the revenues has been prolonged and significant, hence the measure to address revenues has to be prompt and adequate to avoid further irreversible damage.

5. Comment - There is no problem in the telecom sector as Airtel was able to raise money from investors

VIL Response -

One of the stakeholders has commented "Recent interest shown by domestic and foreign investors in Airtel's offering of QIP/FCCBs shows that TSPs are perceived to be good investment with long-term viability. So, all the press reporting about their bad financial health seems to be only posturing to get maximum government concessions". We disagree with this and have the following to say:

- Airtel is one of the first mobile operator in India having started services in 1994. Even after more than 25 years, if it needs to raise money from investors to pay off the liability then it clearly reflects the health of sector in a very poor light. More importantly the other point which is totally missed in the above comment is that Airtel was forced to do this fund raising with in a period of 8 months after raising a large sum of Rs. 25,000 crores through rights issue in May 2019.
- Factors like possible VIL's exit if floor price issue is not addressed promptly in a reasonable manner, thereby leaving Airtel as the only operator that can provide 2G and 4G would have weighed in mind of the investors. Thus any such ability due to possibility of becoming monopoly should not be considered as a factor for the competition and it's not in the interest of the consumers.
- Airtel in its submission has said "Over a 4 year period, Airtel has seen no revenue growth but a massive 80,000 Crore of Capex to cope with the surge in traffic. This has led to significant deterioration of financial health as reflected in the net debt to EBITDA position."
- The comment stating "all the press reporting about their bad financial health seems to be only posturing to get maximum government concessions" is surprising and clearly reflects that the comment is casually made without actually looking at the financial statements, specially over the last 2 quarters where both the company and the auditors have expressed concerns about the going concern ability of the company. Anyone who understands financial statements can vouch that at the leverage ratios for FY19 stands at 21.8x for VIL and 4.1x for Airtel, being the two remaining private incumbent operators, there is genuine stress. The fact that as many as six operators had to exit the industry since the launch of services by new operator with free services in 2016 is a testimony to the fact that the stress in the sector is real. Enough damage has already been done. A further exit would drive the industry to monopolistic situation with the consumer being the ultimate loser. It is TRAI's role to ensure that we do not head in that direction.

We do not believe that anyone should wait for any further TSPs to file for bankruptcies before a view is taken on the matter. In the past, RCom and Aircel have filed for bankruptcies and four other operators have exited by selling their businesses to other existing operators.

6. Comment - Apprehensions regarding some operators making a windfall gain

VIL Response -

A few stakeholders have expressed apprehension regarding some TSPs making windfall gains.

We wish to reiterate, a floor price would be an interim measure towards ensuring viable tariffs and dynamic efficiency (markets should be competitive and efficient over a period of time and not just at a particular point of time), which would result in consumer benefit and social welfare. As mentioned in TRAI's consultation paper and VIL's comments, floor price has been introduced in some other countries. This situation could for the temporary period result in a short- term higher return to certain operator(s), but that is an acceptable situation in the overall interest of maintaining health of the industry as it would create a more stable and vibrant competition in the market over time..

In this context it is noteworthy that **Business Today report[2] dated February 27, 2019 quotes a report by Brokerage Bernstein and has suggested that even the TSP that has reported profits may be losing money and thereby earning a negative rate of return. As per the report, the preparation of account relies on non-standard depreciation metrics and that all the handset metrics are being booked in another group entity. If this were the case, then the possibility of any TSP making a windfall gain is remote.**

In past few years the industry has witnessed structurally damaging developments like completely free services for acquiring a large subscriber base and market share gains, pre-launch connections provided to public for free, voice announced as truly free and later charged for off-net calls, and a number of other situations that have led to present major tariff related financial problems for the industry The industry needs to develop into a more stable situation with growth possibilities emerging from a healthy competition. The floor price is essential to provide such stability and window to move towards such a situation.

Without a floor price and a stable period to move toward healthy competition, the financial distress could create a virtual monopoly like situation with a much longer period of windfall profits for the remaining operators due to absence of effective competition.

The large debt of operating companies or even the parent company of the leading player would indicate that investments have come at huge cost and impacted financials.

TRAI can review the impact of floor prices after seeing the results post completion of a reasonable period of time from the effective date and thereafter on a periodic basis. If TRAI comes to a conclusion that players are making a windfall gain, then TRAI can take appropriate measures to address the same. In certain markets like Bangladesh, in order to handle unprecedented share of market of the leader, for a temporary period, the regulator introduced floor pricing only on the market leader. Therefore, through timely review and intervention, any possible windfall gains can be dealt with by regulator. But at the moment, ensuring sector health and adequate players is the need of the hour and hence needs to be decisively addressed by pegging floor price at the right level to ensure that existing few operators can exist with at least breakeven level covering all costs including cost of capital and be able to invest in networks, services and operations.

It is noteworthy in this context that one of the TSPs in India, i.e. the public sector service provider, is already being financially supported by the Government.

7. Comment -Prices with respect to the per capita income in PPP terms are high and not low

VIL Response -

A comment has been made that :"In PPP terms Indian data tariffs are higher than developed countries. We pay higher percentage of our per capita income per GB of Data for a relatively

[2] https://www.businesstoday.in/top-story/jio-could-lose-rs-15000-crore-this-fiscal-year-bernstein/story/322724.html

lower quality of data." However, no data or the basis of coming to this conclusion has been provided in support.

Furthermore, this comment is based does not reflect the complete basis of the concept of PPP. In PPP terms, the Indian GDP per capita is almost four times the nominal GDP. This happens because of the lower relative prices of the consumption products for Indians, which changes the "effective" purchasing power of our incomes in US$ dollar terms compared to the nominal value. Telecom tariffs are amongst the lowest in the world, and very significantly lower than the US tariffs for example.

In this context, TRAI's statement in the consultation paper (Clauses 2.2, 2.5 and 2.6) that the data costs in India are the lowest in the world, is highly relevant and points to the incorrect understanding by the comment on PPP.

If India's data tariffs that are high on a PPP basis, then the question is why does India have the highest per subscriber consumption of data?

It is highly relevant that the financial distress faced by the telecom industry will not vanish if calculations are made in PPP terms. The TSPs that have exited the industry would not have stayed behind based on a calculation involving PPP. The comment also does not reflect the situation of financial distress in the industry.

Further, with due respect, we submit that making PPP adjustments may not be the correct way to evaluate tariffs. For tariffs to be compared on a PPP basis, the costs for providing telecom services in India should also be lower to the extent of the PPP difference. However, this is not the case:

- As TRAI would appreciate, telecom services are a capital-intensive business and telecom equipment comprises a significant part of the capital and operating costs. Telecom equipment suppliers comprise global players. Prices paid by Indian TSPs are based on the global forces of demand and supply for telecom equipment and Indian TSPs pay the similar prices as in other countries. In fact in Oct 2018, custom duty has been increased from 10% to 20% on many components of active infra required for 4G rollout. This adversely impacted all TSPs except one, where due to the FTA arrangements, the respective imports are exempt from such duty. This is in line with the prices that India pays for commodities like petroleum gold and other metals. They are not lower in India because PPP per capita in India is lower.
- Similarly, on a PPP basis the spectrum costs in India are much higher than anywhere else in the world. According to a paper by GSMA on spectrum pricing in developing countries, "the cost of spectrum (on a MHz basis) as a proportion of income was around 2.5 times higher in developing than in developed countries between 2010 and 2013, then increased to around 4 times higher than 2014 and 2016, before returning to 2.5 times higher in 2017. The spike in the developing countries prices between 2014 and 2016 is mostly due to a number of expensive assignments in India, Iraq, Pakistan, Niger and Afghanistan"
- TSPs also incur very high energy costs. Energy costs are high in India and are not impacted by factors which lead to a higher income estimate in PPP terms.

- Costs of the industry are also a factor of the regulatory levies and policies of the country. It may be noted that in China, the only market of a comparable size as India, spectrum is given for free to operators and there are negligible regulatory charges. The floor prices proposed by VIL in its comments are much lower than the current data realisation in China.

Crux of the matter is that revenue has to be commensurate with the cost whether in nominal terms or PPP terms. Evaluating only one of them on the basis of PPP may not be appropriate. Ultimately, revenues have to be commensurate with costs, and the financial distress is not a situation which will go away if a different exchange rate (i.e. calculation in PPP terms) is applied to the underlying numbers.

In any case, the same stakeholder has later provided comments strongly holding need of the floor price fixation and it being need of the hour.

8. Comment - Floor Price does not comply with international best practices

VIL Response -

One apprehension expressed by a few stakeholders is that Floor Tariff may not comply with international best practice. In this regard, following may be considered by TRAI:

- There is no best practice in such exceptional circumstances as these are absolutely uncommon. Hence, floor pricing is a commonly accepted economic principle in these circumstances and there are international precedence covered in the consultation paper; it is also mentioned and in certain instance applied in the TRAI's Telecom Tariff Order 1999, which began the major tariff reform in India. In fact, the deep distress is the result of delayed action to address the issue of below cost pricing which has prevailed for long, creating an unsustainable financial position of TSPs in India.
- The telecom sector in no other country has witnessed similar revenue decline and surmounting losses as the Indian telecom sector has over the last four years. There is no other comparable market in the world, where each and every TSP who was operating before 2016 has either exited or if surviving is incurring significant losses.
- The ARPUs in other countries are much higher, even though equipment costs tend to be similar across the world.
- We do not know of examples of developed markets where all but one operator is losing money at an EBIT level. Also, the profitability of that one operator is based on different accounting practices and if calculated in the same manner as other TSPs, the result could be different as is borne out by the Bernstein report referred to earlier.
- The rates of return in developed markets are in sharp contrast to the numbers for Indian TSPs. As an example, rate of return on equity for leading wireless telecom service of US are much higher. As mentioned previously, **in Europe, concerns are being raised over returns below 10% with ETNO's report stating that such low levels of return are "clearly not a sustainable or desirable position for operators".** With several TSPs having exited the market in recent years due to financial stress, and most remaining TSPs earning negative returns, the situation is much worse in India.

- Additionally, another key difference between Indian telecom market and the sector in other countries is that the cost of spectrum in India is significantly higher compared to most of the other countries. The large spectrum commitments made by the operators over last few years have resulted in the ballooning debt levels. **In comparison, in China which is some ways is the most comparable market to India in terms of size, spectrum is given free to all three TSPs, and the regulatory charges are insignificant and despite that the ARPU in China is around 4 times that of ARPU in India. That clearly shows that the prices in India are way below costs.**
- India is a unique market. It is an established fact as it has the lowest prices in the world and the highest per capita consumption of data. Therefore, a unique situation and unique market requires an appropriate solution. Other countries when faced with economic challenges find their own solutions. In United States, there is a history of Government intervening in sectors with high financial distress. As an example, the US Government intervened to provide protection to automobile companies in 2009. Therefore, Governments and regulators look for what is best for their country.

9. ***Comment - Hampers competitive efficiencies in market by hampering allocative, productive and dynamic efficiencies by artificial/external intervention***

VIL Response -

Apprehension has been expressed that Floor prices will hamper the competitive efficiencies in market by hampering allocative, productive and dynamic efficiencies by artificial/external intervention. In this regard, it is submitted that:

- Implicit in the comment is the assumption that currently prevailing prices are appropriate just because they are market determined. Market determined prices are however not always pro-competitive as has been recognized by competition law. For instance, in case of predatory pricing, competition authorities recognize that even though prices are lower in the short-run and thereby benefit consumers, the possibility of lower competition and higher price in the long run implies that such pricing is anticompetitive.
- A similar outcome may emerge in the telecom sector if current unviable pricing practice continues and TSPs are forced to exit the market (as many as six have already exited in recent past due to financial stress).
- Further, the observation assumes that the telecom sector is a well-functioning market and thus a regulatory intervention would be inefficient/result in a suboptimal outcome. Factors such as the current price war like situation in the sector and the financial stress faced by TSPs and its likely outcome on the sector has not been taken into consideration.
- The floor price is being proposed only when current price despite some recent increase is such that it is influencing basic viability of the sector. If the market determined price is viable, TSPs will be free to determine their own price. It is only when the price, being below cost, affects financial viability that the floor price will kick in.

Therefore, a key issue with this comment that it is theoretical. A dynamic, forward looking approach which takes into consideration the long term implications of the current situation persisting in the telecom sector has not been considered. For instance, they comment on the important role played by the telecom sector in the economy and how a price floor and resulting tariff hike would have an adverse effect but don't analyse how this scenario would compare to one where TSPs exit the market and competition decreases and prices increase due to inadequate competition in the market.

10. Comment -Timing of the introduction of floor price

VIL Response-

There have been suggestions that Floor Price should be introduced in a gradual manner.

The request for floor price is being made to address the immediate financial stress on the TSPs, who are incurring huge losses. Details of the losses have been provided in our previous submissions. Even the recent increase in tariffs have been inadequate and losses are continuing. Therefore, we suggest that the Floor Prices be implemented at the earliest. **Any period of introduction like 6-9 months is not workable at this late stage where the AGR related liability has increased the financial stress, which will result in irretrievable damage to the sector and will see exit from an already depleted set of players. Such a delay will be neither in the interest of the consumers nor even of the Government. The objective of stabilising the market would not be achieved. It is reiterated that the objective of floor price fixation should be the revival of the industry. Therefore, any half measure taken with respect to either rates or timing will not result in such revival but in exits which in turn will result in deprivation of connectivity to a large subscriber base. As said by one Government stakeholder, in the extraordinary circumstances that the sector is going through at present, floor prices are absolutely necessary to avert lasting damage to India's digital agenda and economic growth.**

It is also important to note that the need for floor price has been there for a long time and it was first discussed in July, 2017. If it was introduced much earlier, a gradual approach could have worked. The financial stress is acute and has further worsened post the crystallization of AGR liability which has seriously impacted the industry. At this stage a gradual implementation will be a case of "too little too late" and the objective will not be achieved. A gradual implementation will result in irreversible damage in the form of further exits and marginalization of the sole government operator who may continue with government support, but would not be able to cover its costs at sub optimal floor price.

11. Comment - Have the recent tariff hikes been adequate or not

VIL Response -

In some comments, a question has been asked whether in light of the tariff increases in December 2019, is there a need for floor prices. This issue was raised in the Consultation Paper issued by TRAI and has been addressed at length in our detailed response submitted earlier.

12. Who should the Floor Price be applicable on?

The intent of the Floor Price is to help stabilise the market by restoring the financial health of the TSPs. There has been a suggestion that Floor Price should be applicable only for TSPs with a greater than 15% market share. The rationale for this recommendation has not been explained. This suggestion of exempting TSPs with less than 15% market share for Floor price is not supported by VIL.

In any case, Floor Price should be applicable to all TSPs and should ensure that the financial health of the industry is restored.

13. Methodology for computing floor price

In addition to the suggestion made by us, the following suggestions have been made by others with regard to the computation of the floor price.

- One stakeholder has suggested that there be a staggered increase in tariffs i.e., first to Rs.15/GB and then Rs.20/GB. They have said floor should not be based on cost but investment and have then mentioned a number of Rs.20/GB.
    - While the outcome (Rs.15 and Rs.20) has been mentioned, however how the floor tariffs would be computed and what is the basis of the numbers quoted has not been stated.
    - The rationale for asking for a Floor Price is to alleviate the financial stress of TSPs. Therefore, **any methodology that does not consider the current costs and capital already invested in the business of the TSPs may end up with outcome that does not relieve the financial stress. The whole objective of introducing floor prices will be defeated.**
    - It has been suggested that floor price computation be linked with the future investments needed. The financial situation will depend more on current costs rather than future costs. If current costs are not covered, future investment will be very difficult for TSPs under major financial distress. Future investments should be considered only after the Floor tariffs ensure that the current costs of the TSPs and a reasonable return on capital invested till date is provided to ensure that there is adequate competition and the possibility of a future virtual monopoly is minimised. In any case the floor price proposed by VIL is based on current costs and if future investments of a large nature for 5G etc. are considered, that can only increase the overall costs and require a higher floor price.
    - Further, there would be subjectivity involved in estimating the timing of future investments. Future investments will be made only by those TSPs that are not forced to exit the market, due to the financial stress.
    - The basis of future investments will be a double whammy for the consumers as firstly, it will not resolve the current financial stress and therefore any such rate will lead to exits and in virtual monopoly, and secondly, the said operator being a virtual monopoly will be given additional benefit of floor price in such a situation. Thus,

this justification, in the present given situation, is unreasonable and will lead to far more damaging results.

- VIL reiterates the following methodology for the floor price:

  a. List down all the costs

  b. Add the figure of cost of capital @ 15%

  c. Gross up the return on capital for license fee and SUC on incremental revenue required to cover these items

  d. Reduce voice contribution in bundles @ 6 paise / minute for outgoing calls (offnet & onnet)

  e. Take actual revenues for all other non-data services (including metered voice and IUC Revenue on incoming calls) and deduct the same from total costs, then add License fee and SUC cost on the higher revenue required to arrive at the cost which has to be recovered by way of data floor price.

  f. Divide the cost attributable to data plus the cost of capital as the revenue required to achieve the objective of covering all costs.

  By this methodology the cost comes to Rs 42.9/GB (excluding GST). Floor Price structure with Subscription Fee is proposed as follows:

Elements of Floor Price Structure	**Floor Price (excluding GST)**
Offnet Voice Floor Price (Rs per minute)	0.06
Minimum Subscription Price (Rs) per plan period of 28 days for prepaid and one month for postpaid	
Voice only Subscriber	40
Data only Subscriber	50
Voice and Data Subscriber	75
Data Floor Price Rs / GB	**35**

Further, there should not be any discount on offerings having validity of less than 84 days. For long validity plan following approach should be followed:

Plan Validity	**Maximum Discount**
Less than 84 days	No discount
84 days or more upto 168 days	10%
More than 168 days	15%

Airtel has proposed a telescopic pricing model. However, the telescopic pricing is resulting in significant decline in cost recovery compared to a flat price model and as a result cost of capital is not being fully recovered.

VIL submits that telescopic pricing can be an option for floor pricing, however, to achieve the right result, there is a need to have the slabs of telescopic pricing at both the higher and lower level than a flat price of Rs.35 per GB. Hence, VIL proposes the following slabs (all excluding GST), which based on our assessment will give the same weighted average data realization of Rs.35/GB proposed for a flat floor price.

Up to 5 GB per plan period (i.e. 28 days)	Rs.40/GB
5-15 GB per plan period	Rs. 30/GB for data exceeding first 5 GB per plan period
Over 15 GB per plan period	Rs.20/GB for data exceeding first 15 GB per plan period

A flat floor price for data gives an overall lower cost to low volume users, but results in the same cost applicable to high volume users. As against this a telescopic price results in a higher price for low volume users, but provides benefit to the high volume users. Both methodologies have their merits and drawbacks. **It is for TRAI to decide which one is best suited for the Indian market situation. However, what is essential is that irrespective of the choice of model the end objective of recovering all costs including cost of capital should be similarly achieved**.

On Approach 3 of proposed by Airtel, it is submitted that the daily limit plans are the key reason for the current state of the industry, where while data consumption has grown exponentially, but the Revenue of the industry has declined over a prolonged period. The issues with this structure even in the new price proposals proposed by Airtel under this approach are as under (all values excluding GST) –

- Price for 1 GB plan - Rs.165
- Projected price for 7GB plan - Rs.345
- Price for 1 GB/day (28GB/ plan period) - Rs.349
- Incremental price for 27 GB - Rs.184
- Implied price per GB - Rs. 6.8 / GB

The price of 7GB plan under Approach 1 of Fixed Price Model of that Operator is Rs. 345. This means that anyone with a consumption between 7 GB to 28 GB will pay the same price of Rs.349 per plan period. This is against the principles of economics which requires that a consumer needs to pay higher for higher use. This will again lead to a situation which we have witnessed in the past, where operators have made significant investments to create capacity to support the growing traffic, but the revenue did not grow because of this uneconomical price structure. In fact these pricing structures have also driven wasteful consumption to a large extent, as consumers try to consume more and more within their entitlement, as there is zero cost implication of consuming more in such plans. In our view if these plans are continued any further, the industry structure will remain compromised and industry will not recover from the deep financial stress that it has landed into.

The need for a lower per unit price for high volume users can be well addressed through telescopic price as already discussed above. We do not need the price model structure which has a constant price for a wide range of usage (7GB to 28GB) and which has caused significant damage to the industry already, reflecting in large leverage in all balance sheets.

- Other Stakeholders have recommended that Floor Tariff can be determined based on the actual cost of TSPs and a reasonable rate of return on capital deployed (i.e.15%).

14. Rate of return on Capital Employed

Stakeholders have recommended that the rate of return on capital deployed be computed at 14 to 15%.

- Stakeholders have pointed out that 15% rate of return on capital employed is a past precedent of TRAI.
- One TSP has also provided two alternative computations of Floor Tariffs by considering for ROCEs of 10% and 8%. It may be pointed out that both 8 and 10% are lower than the average bank lending rate in India of 11.5% (details provided in our comments to the Consultation Paper). Therefore, Floor tariffs determined on the basis of 8 or 10% ROCE would not be adequate to address the financial distress that the sector is facing. The higher ROCE of 15% has been used by TRAI earlier, and this rate would provide the stability and return that is required to recoup the situation when the industry recovers from the major financial distress that it is presently experiencing.
- The industry is already finding it impossible to attract capital. Also the industry needs to generate adequate cash to deleverage the heavily leveraged balance sheets and also generate a surplus to invest in new technologies eg.5G. In fact to address the damage which has happened in the recent past, the right thing to do is to fix the floor price at a higher than normal cost of capital to enable the industry to deleverage. A floor price based on lower than 15% cost of capital would mean continued losses, inadequate cash generation from the business and inability to attract capital from other sources. In fact some banks have mentioned that they will not provide funding to telecom companies for 5G, given the extent of NPAs in the banking sector because of the current situation of the industry.

15. <u>Costs to be considered for computing Floor Tariffs</u>

Practically all comments made on the costs to be considered recommend that actual costs of TSPs should be considered. There is little ambiguity in this approach.

Related question is, which Operator’s cost should be considered. There are primarily four options:

1. Consider the minimum cost of data incurred by any TSP
2. Consider the average cost of all operators
3. Consider the cost of TSP with the highest or the second highest cost structure
4. The sector regulator should ensure that the Nth Operator (N being the minimum desirable number of operators) is also able to make a reasonable return and sustain their business.

The objective of the floor price is to relieve the financial stress in the sector and ensure that there are adequate number of TSPs, so that customers’ choice and competition is ensured. It may also be noted that globally, countries now find it impossible to increase the number of players in their market for ensuring competition. Option 1 would not provide the operational comfort and possibility for more than one TSP to operate with profits. This would result in a monopoly situation. The objective of the floor price is to give support for a limited period of time to the TSPs to emerge stronger with new investment and initiatives that improve their cost and operational efficiency. Option 2 is not advisable because a simple average could theoretically result in only one or two TSPs (as the average could be lower than the costs of two or three operators).As provided in the Table 1, in case of any further exits, consumers would have to choose between two TSPs for any service (2G/ 3G or 4G) in any geographical area of India. Ensuring that disruption is not caused in an already distressed industry as a result of the exit of the TSPs is an important regulatory objective.

We also wish to bring to your notice, comments of one organisation and two consumer advocacy groups are identical.

We thank TRAI for this opportunity to provide our counter comments.